RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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Aug. 30, 1995 **LETTER 1181**

THE PICTURE: I've never in 50 years of watching markets seen anything quite like the current situation. By any reckoning, this bull market is ancient, long in the tooth, and defying all sorts and varieties of odds. For example, the broad market, as measured by the S&P, has risen in 17 of the last 20 years. This has never happened before during any 20-year period in stock market history. Consider this -- in the last 12 years, the Dow has never closed below a previous year's close. Unprecedented. And over the past four years we haven't had a Dow decline of as much as 10%. Again unprecedented. And we have to go back 21 years, to 1973 and '74, for the last back-to-back yearly declines in the market.

Stockholders are now more thoroughly inculcated with the philosophy of long-term "buy-and-hold" investing than at any time in history. Today, the idol of the investment world is Warren Buffett, America's second richest person. Buffett is famous for taking large positions in favored stocks and holding them "until the cows come home." Two books about Buffett have been published this year; another one will be out shortly. A number of funds have been started, each seeking to emulate Buffett's investments.

I have always known that "the stock market can do anything," and certainly that venerable adage is proving its validity today. The fact is that this stock market is doing things that have never been seen before. One is merely the sheer persistence of its *uncorrected* upward climb.

Robert Rhea, the great Dow Theorist of the 1930's, observed *that every movement in the market -- primary, secondary and minor -- is ultimately corrected.* And all my market studies confirm Rhea's observation. So referring to the current situation, it's not a question (at least in my mind) of if this great bull market will be corrected, it's simply a question of WHEN.

A number of items are worth noting at this point. The first is that the British stock market (the "Financial Times 100") rose to a new all-time high last week. This occurred even though the pound sterling turned weak over the past month. Historically, the British market has turned down *ahead* of the US market (at bull market tops), but historically the US market has turned up (from a bear market bottom) *before* the British market does. The fact that the British stock market is still making new highs is a positive for the US market.

The second item is a negative. It is that volume on the NASDAQ is now running considerably *higher* than NYSE volume (see page 2 chart). This is further evidence (is any needed?) that speculation is rampant and that "investors" are turning increasingly to the secondary stocks for their action. By any reckoning, this is a frothy, overvalued market. But then, it's been overvalued and rather frothy for the last three years, so it's difficult to tell what this latest increase in speculative intensity means.

The third item (see page 2 chart) is that on-balance volume for the Dow turned down at the end of July and is continuing down. This is a negative and implies distribution. Note: on-balance volume is a daily advance-decline line of volume (this is based on Joe Granville's thesis that "volume precedes price").

The fourth item is the CRB Index of 21 commodities on August 21 hit a five year high, led by oil, grains, hogs and silver. The implications of this are that the forces of inflation could be heating

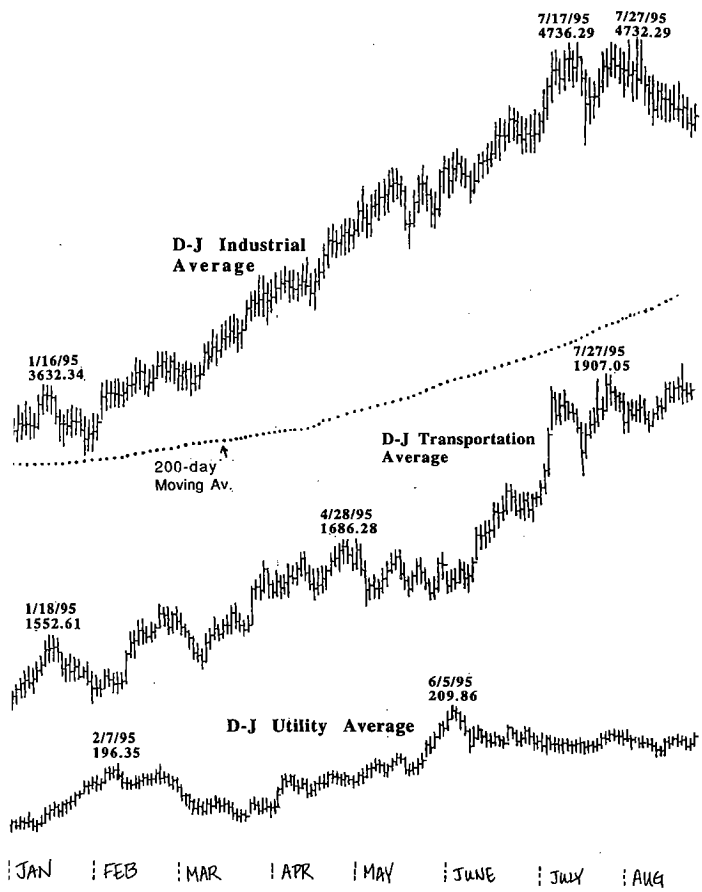
Aug. 18 DJIA 4617.60; PTI 4231; A-D Ratio -4.05
Aug. 25 DJIA 4601.40; PTI 4237; A-D Ratio -3.95
Dow Yield: 2.50%; Dow Price/Earnings: 14.3
Dow 200-day MA: 4198; Dow 30-day MA: 4662
Dow Times Book Value: 3.52; PTI 89-day MA: 4169
Percentage of Undervalued Blue-chips: 5%
Gold 200-day MA: 384.16; Gold-PTI: 724

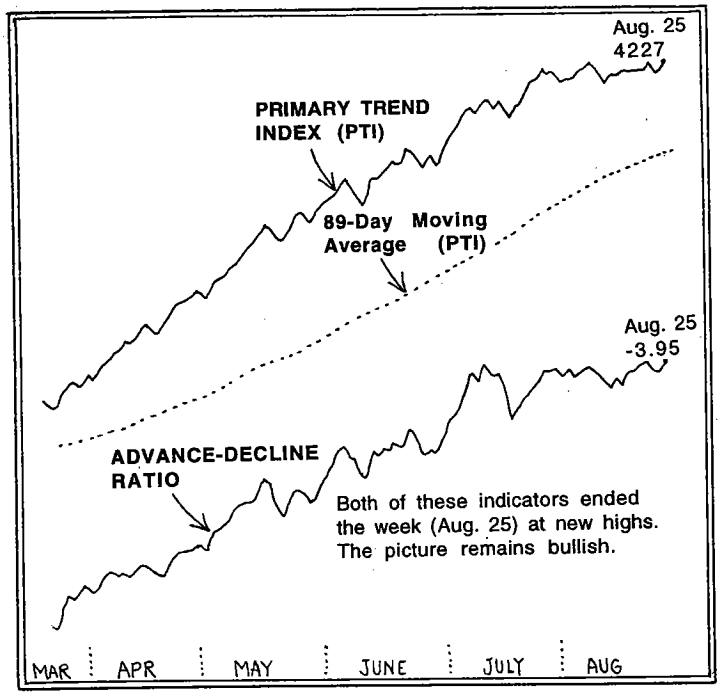
up. If nothing else, this should prevent any easing of money or any forthcoming decline in interest rates. See chart on page 2.

The fifth item, and this is an unusual one, is that the advance-decline ratio (NYSE) hit a new high on August 21, but this high was not confirmed by the Dow. Thus, the broad market appears to be stronger than the blue-chip Dow. Ordinarily, this should be considered a PLUS for the overall stock market. It means that the "soldiers have been outperforming the generals." However, we must remember that the Dow represents investment-grade stocks whereas the A-D ratio represents the advancing or declining trend of ALL the stocks on the NYSE. There have been a number of instances in the past where a Dow non-confirmation of an A-D high has led to trouble. So let's see what happens this time.

Item six: corporate insiders have been moving to the sell side. According to the *Insiders* report, over the last five weeks 64% of insider transactions have been *sales* while only 36% have been purchases. That's another negative for the market.

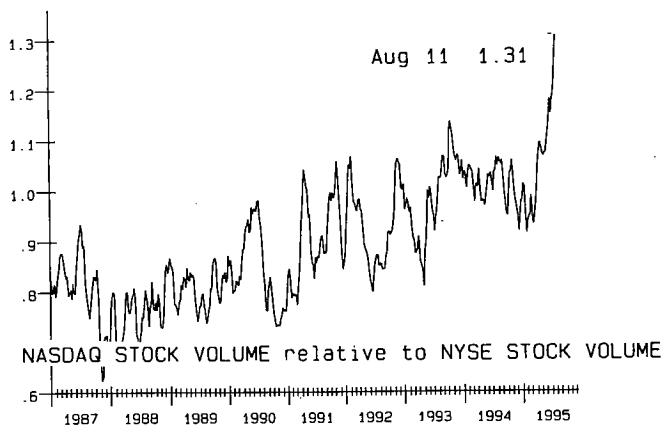
Item seven: I've been doing a good deal of work with daily new 52-week lows on the NYSE (not highs, just new lows alone).

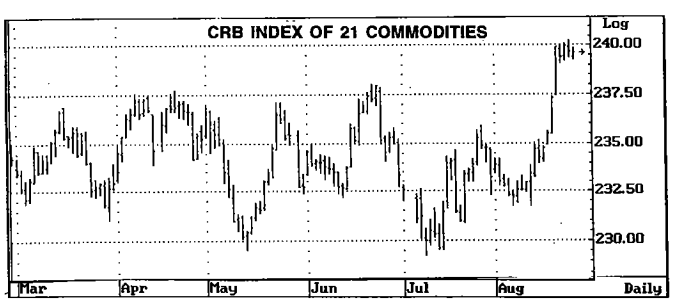


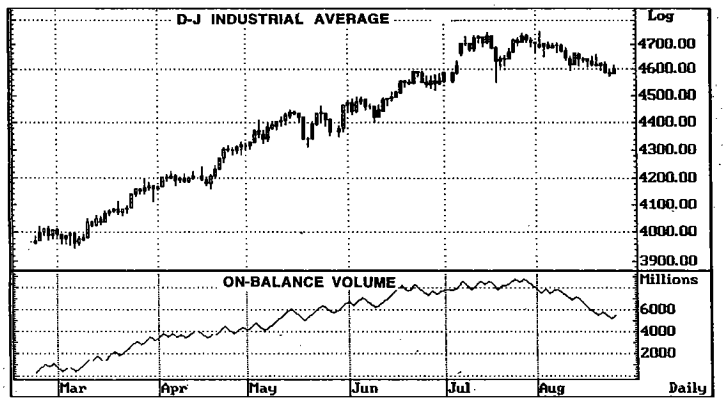


Recently new 52-week lows have been holding in a very low range (3 to 15 a day). However on July 24 we saw a peak of 24 new lows. Watch the daily new low list. A definite indication of important weakness would come on any day in which daily new lows surpassed 24. An expansion of new lows implies increasing selling pressure (conversely, of course, a lack of new lows implies that meaningful selling is absent). At any rate, my studies show that a few days with new lows pushing above **24** would represent a signal that should be taken seriously.

In the end, it's PRICE ACTION to which I give the MOST credence. In my experience I have found that the best single way to track price action is through my own **Primary Trend Index (PTI)**. Therefore, I strongly suggest that subscribers keep their eyes glued to the PTI chart at the top of page 2.







INVESTMENT POSITION: The bull remains in the box . . . Monday morning openings are amazing. It's as if investors can't wait to buy stocks. Every Monday morning starts with an upward surge as weekend buy orders are filled. I don't think I can remember a comparable frenzy to buy (unless it was back in early 1959, but, of course, volume was far lower then, even if enthusiasm was just as intense).

The difference in the current market compared with previous ones is the presence of 5,000 equity mutual funds with carloads of new cash coming into those funds daily. With the public feeling relatively safe in "investing" with the funds, the market has developed a fantastic built-in head of steam.

But there's a downside. To me, the funds mean stocks are in weak (public) hands. We have never seen a bear market with the public this heavily invested in the stock market. Remember, if a fund-holder becomes frightened, all he has to do is call his fund (if he can get ahold of it) and say, "Switch my account into your money market fund!"

All in all, I don't think I've ever seen a more complex situation in the economy or in the stock market than what we have now. Watch the PTI (it's still strongly bullish) for any trend change. Bonds are rallying again (see Late Notes). Silver has moved up, gold has done nothing. But two unusual gold stocks that deal strictly in royalties (Toronto Exchange), Euro Nevada and Franco Nevada, continue to act superbly. I like them both.

TOPS AND BOTTOMS: Market tops tend to be difficult to identify. One main reason is that the big stocks, the type of stocks that are in the Dow, are usually carefully distributed, and this process *takes time*.

This careful distribution often shows on the charts as large head-and-shoulders patterns or as rounding tops or as long lines of distribution. On the other hand, secondary and more speculative stocks often run up in spike formations or in parabolic surges that can end in spearpoint tops.

Thus, a major bull market top may take months or even a year or so to form. The process of distribution, the overpowering of the sellers by the buyers, completes the top and the entire market will then roll over and head down.

The old market adage tells us that "it takes buying to move the market up, but when buying dries up, stocks will fall of their own weight." This is true, and when bull market buying declines substantially, that's when stocks begin to fall of their own weight. If stocks continue to sag, at some point investors become

disturbed and begin to move to the exits. Selling pressure increases, and the bear market is on in full.

There are a lot of technical techniques and formulas which seek to identify a market top, but I have never found one that is particularly accurate. A number of techniques can tell you when you are in the broad area of a market top, but as to pin-pointing the top -- no formula that I have ever seen will do the trick.

Bottoms are much easier to identify. A great bear market bottom is always characterized by very attractive yields on blue-chip stocks. Another way of putting it is that stocks are great VALUES at major market bottoms.

But values alone will not identify the bottom, since great values can become even greater values. There is a little known technique, which is extremely valuable. It was developed or discovered by a brilliant young man that I used to correspond with many years ago. I'm referring to the late Jim Alphier, who worked for Argus Investment Management in Santa Barbara, California.

Jim called his bottom-identifying technique "prolonged liquidation." His original discovery worked as follows (these are his words): "Each week count how many days the S&P 500 closed up and how many days it closed down. If there is any day the index is precisely unchanged, give that day the sign of the previous day. Ignore the magnitude of the rise or fall, and forget about holidays or other days the market was closed. At the end of each week, go back over the past 14 weeks of data. Count how many total days are up and how many are down.

"If, in the past 14 weeks, there are at least 17 more days down than days up, you have an important buy signal. The amount by which the number of down days exceeds 17 (if any) is only of minor importance. When the signal occurs, the investors can rely on other studies (or personal judgment) if fine tuning the exact buying time is important."

Incredibly, the above described technique has identified just about every important market bottom since 1938. This technique works because it identifies areas of extreme pessimism, the kind of pessimism and selling that ends bear markets.

In his report of August 4, '95, market analyst Peter Eliades refers to a later version of Alphier's "urgent selling" technique. This second formula seems to identify secondary bottoms as well as areas of major market bottoms.

The shorter formula works as follows: Any period of 15 days which contains at least 12 down days identifies a period of urgent selling. Using this "formula," Eliades notes that periods of urgent selling occur about every year and a half. He further notes that "several waves of urgent selling may occur near important buying junctures when pessimism is high and when selling is overdone. Conversely, bull market tops occur during extended periods of little or no urgent selling."

Then Eliades makes a very interesting observation. He notes that the *last period of urgent selling occurred back in October, 1987.* Before that, the longest period in this century in which urgent selling was absent was the period of 1922 to 1929. The 1922-29 period was followed by history's worst bear market.

The question is -- what is the meaning of the 1987 to 1995 time span, a period without a single instance of urgent selling? For one thing, the absence of urgent selling over eight years tells us that investors have enjoyed an extended period of persistent and extraordinary optimism. In fact, during 1995 the optimism has given way to literally a "new era" psychology in which neo-experts tell us that reactions or bear markets are phenomena of the past, and that the road to riches lies with the long-term holding of common stocks. Thus predictions of Dow 5000, 7000, and even 10,000 are now common.

Buffett and Templeton and other long-term holders are deified, and the buy-and-hold philosophy is presented as the royal road to wealth. Comfortable retirement lies in buying good stocks and holding them for a lifetime.

Conclusion: The eight-year span (1987 to 1995) without a single instance of urgent selling has only happened once before in this century. The last time it occurred, it was followed by the 1929-32 stock market debacle. A commonly heard expression regarding the 1995 market is that "this time it's different." Remembering what happened the last time urgent selling was absent for years, let's hope, therefore, that this time it really will be different.

NEW, NEW: A few months ago I announced that I had started a new business. Subscribers were free to write in, requesting information about the new business. To date I've received well over 2,300 inquiries about the business, and over 100 subscribers have elected to participate. If you're interested, feel free to find out what I'm doing. Just drop a card or a letter (PO Box 229, La Jolla, CA 92038), and you'll receive what I feel is interesting and informative material. No cost, no pressure, no gimmicks, no follow-ups.

NOTES & QUOTES: August -- hype month: first the super-hype of the Tyson-McNeely non-fight. Then the magna-hype of Windows 95, the new Microsoft software which is supposed to make Windows more like Mac. My only question -- if Windows 95 is so simple, why are there over 400 books and pamphlets coming out explaining how to use it? Note: pirating has become a major problem -- for weeks knockoffs of Windows 95 have been selling in Hong Kong for four dollars.

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Watch this area -- the Mexican peso, propped up by billions of US dollars, has been slipping again. Late reading is 6.40 to the dollar. If the peso drops to 7 or more to the dollar -- trouble.

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The chairman of the House Budget Committee, Rep. John Kasich (R-Ohio) is intent on balancing the federal budget. He says that his "worst nightmare" regarding the coming budget confrontation between Congress and Clinton is that the Republicans will blink. Says Kasich, "My nightmare scenario is we will all wink at one another across the table and that we'll sell the American people a pig in a poke and walk away and not have changed anything." Here's the coming drama -- by October 1, the national debt ceiling must be raised above its current $4.9 trillion. Only Congress can do that. Says Kasich, "It's up to the President as to whether he wants to recognize the results of the '94 election. If he doesn't want to, then I guess the government's going to get closed down." In other words, if Clinton vetoes the Republican budget, all hell will break lose. "We're not going to raise the debt ceiling until we get a deal. . . until we get an agreement on a deficit-reduction plan," warns Kasich. So if Kasich is right, either the Republican budget goes through or the government runs out of money and is shut down. **Russell comment:** Should be interesting around the end of September.

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By the way, the latest additions to the national debt (over the last 12 months) was $313 billion. This is the highest addition of the year. It means that this nation is adding the national debt at the rate of almost one trillion dollars every three years. Against this, the Treasury announced that the deficit was being reduced. Who's kidding whom?

* *

The two Michaels, Ovitz and Eisner, the two most powerful men in Hollywood -- together at last. What does it mean? It obviously means that Disney is the most powerful entity in Hollywood. Ironically, Ovitz, as agent, was one of the men who was responsible for pushing star salaries through the roof, but Ovitz is now on the other side. The feeling is that power is now passing back to the movie producers and away from the agents. Well, that's the theory, anyway.

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Subscriber W. David Stedman of Asheboro, NC., is that rare person, a patriot who actually does something for his country. David has just published a marvelous 83-page glossy-paper book

entitled, *"Rediscovering the Ideas of Liberty."* The book is a treasure trove of information on the Constitution, on the Founding Fathers, on money, property rights, trial by jury, freedom, separation of powers, plus much more. The book deals with fundamental laws and ideas that every American should be aware of and understand. To my mind, the greatest danger to this nation is to be ignorant of our Constitution. The Constitution is our great gift of freedom, and our bulwark against government tyranny. The paper-cover book is written in clear, easily understood English. I recommend it to everyone (paper bound and very attractive). Price is $15 delivered anywhere in the US. [(800)USA-1789, or Stedman Associates, Publication Division, 1438 East Dixie, Suite 100, Asheboro, NC 27203].

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A terrific article in the September issue of *Esquire* accuses Hollywood of turning into one huge welfare machine. The article states that underlying Hollywood is *"a system in which featherbedding is endemic, responsibility is nonexistent, risk taking is discouraged but failure is nevertheless rewarded, huge salaries have no discernible relationship to profits, and corporate revenues are used as a slush fund for personal gains."* The article describes Hollywood's revolving door where executives, even if they are incompetent or non-productive, move from one high-paying job to the next, protected by friends and cohorts in the industry. **Russell Comment:** Before you decide to be a producer or before you invest in Hollywood, I strongly suggest that you read this article. Friends in the industry tell me that this article is "right on."

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The Republicans are finding that it's not that easy to push their Contract With America through first the House, then the Senate, and finally to avoid a veto by Clinton. As a matter of fact, very little of the Contract has been put into law (actually, only two out of the 10 items have passed into law so far). One of the problems is the ideological divide between the more liberal House and the more conservative Senate. Ironically, Clinton has become the status quo president. He threatens vetoes on the Crime bill, the Regulatory Reform bill and the Legal Reform bill.

But make no mistake, Clinton's main skill is in campaigning. And he never stops. He's now putting in one of the earliest and most aggressive campaigns ever -- and the first goal seems to be to scare off possible Democratic challengers (read Jesse Jackson). Clinton's group has already collected $10 million for the campaign with a goal of twice that.

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Speaking of Clinton, he and Hillary have amassed $1.6 million in unpaid legal fees, amid a sharp drop-off in donations to their legal defense fund. The Clinton Whitewater bills total $1,143,987 so far. Clinton owes Bob Bennett's firm $680,000 (the firm represents Clinton's sexual harassment case). And the president's Little Rock firm is owed $62,000 for work on Whitewater and sexual harassment. Yep, he's one busy president.

* *

I continue to hope that M. S. ("Steve") Forbes, Jr. will run for president on the Republican ticket. I firmly believe he's the only candidate who understands the economy. Forbes is openly for the flat tax, for an end to the IRS, and for a gold connection to the dollar. Forbes is a multi-millionaire, has never run for office, and is extremely intelligent and well informed. Steve, go for it -- you've got my vote.

* *

The Aug. 21 issue of *US News and World Report's* cover story is, "The Man to Watch, Colin Powell." The story goes, "As Americans grow more disenchanted with their leaders and with both politician parties, Colin Powell is seriously considering an independent run for president. The problem is that nobody has any idea of where Powell stands or even whether he would be a Republican or a Democrat." Powell spoke here two weeks ago, and friends who heard him told me, "He's very charismatic, a very good speaker, says all the right things, tells us that the US is 'a great country,' talks about 'everybody getting together,' says nothing controversial." Powell may be the perfect politician (like Eisenhower), but I'm interested in knowing what a man stands for. Both parties would love Powell as Vice President. As President? That's another story.

* *

It still amazes me how far this nation has gone towards destroying its money. Back in 1896 the US was subject to a gold standard, at which times there was a parity between the US dollar and the British pound. There was roughly five dollars to a pound, and four pounds were equal to one ounce of gold. At that time, the dollar was both a store of value and a vehicle of commerce. In recent years the dollar has become strictly a trading vehicle. Nobody sees the dollar as a store of value.

Today, the sophisticated investor cannot keep his wealth in dollars for very long. He must constantly seek to increase his wealth in order to offset inflation and the decline of the dollar. This has generated global interest in trading currencies. The major currencies now trade on the Interbank (or GLOBEX) at the rate of at least one trillion dollars a day. **Comparisons:** in 1970 a dollar was worth 360 yen or 3.6 marks. By July 1995 a dollar was worth only 88 yen or 1.4 marks. That represents a dollar drop of 76% against the yen and 61% against the mark.

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The latest issue of *Worth* magazine has a most interesting article on John Gutfreund, former head of once-mighty Salomon Bros. Gutfreund married an ambitious young woman, and got caught up in the social whirl. During his "reawakening," he may have neglected his job at Salomon, we don't know. But when Salomon ran into trouble, board member Warren Buffett stepped in and took over. Buffett ousted Gutfreund, and even prevented him from receiving severance pay. After reading the whole story, I felt rather sorry for Gutfreund, and I also felt that Buffett was one tough, unforgiving fellow. Mess with Buffett's money and brother, you're history.

In the same issue of *Worth* there's an article by Peter Lynch (famed former manager of Fidelity's Magellan Fund). Says Peter, buy and hold and forget about bear markets, since you never know when a bear market is coming. Conceding that bear markets are a fact of life, "How can we be prepared?" Says Lynch, "Mostly by doing nothing." Agree with Lynch or not, that's the prevailing psychology of today.

* *

The latest (Aug. 25) issue of *Forbes* magazine features mutual funds. The cover offers info on the "Best Funds," "How Many Should You Own?", "Buy a Family, Not a Fund," and "1,801 Funds Rated." **Russell comment:** How's that, 1,801 funds? There's no craziness like Wall Street's craziness. But Wall Street's genius is in its ability to make its nutty fads appear logical. And Wall Street, somehow, has the ability to take its own hype seriously.

* *

The dollar's sudden strength will impact on the big exporters, companies that comprise many of the Dow industrial stocks. The authorities in both Japan and the US were afraid of a possible meltdown at the big Japanese banks. And of course, such a meltdown would have rubbed off on many US banks. So intervention in the currency market boosted the dollar while it whacked the yen. The FOREX (foreign exchange) traders saw the picture and went with the trend. Fortunes were made over the last month betting on a collapse in the yen.

* *

Dominick Dunne, in the current issue of *Vanity Fair*, writes about "The Case Against O. J." To me, the evidence against O. J. is overwhelming. Why Judge Ito allows the defense to go on and on with the ridiculous racist conspiracy against O. J. is beyond me. The whole trial has deteriorated into an endless, goofy bore. Even O. J. with his various weird facial expressions is beginning to look goofy. Confession -- I've stopped watching the trial. Football is starting. Ito, get on with it. The case is already over. The outcome will be an exhausted, hung jury.

* *

I switched to the fast pentium computers last year plus the Power PCs for my Macs. But no sooner do you load up with the latest computers and software, than an even newer series emerges. By year-end Intel will be shipping its latest hot chip (hotter than the pentiums), the P6. The P6 will leave the pentiums in the dust when it comes to running advanced 32-bit software. The estimate is that in '96 Intel will ship eight million of its new P6 chips. The forecast

is that 54 million PCs will be sold this year and 20 million of those will have pentium chips. One problem -- what do you do with old PCs? They are not bio-destructible. And already there are great mountains of them. Will they soon cover the world?

* *

Fare on the NYC subways is going up to $1.50. I find it hard to relate to a $1.50 subway ride. When I was in high school it cost me a nickel to ride from home in midtown Manhattan to my high school 25 miles away in Riverdale, NY. Or at the age of 15 I could ride from my home in Manhattan way out to the end of the line in Astoria to the wonderful 1939 World's Fair -- all this for a nickel. Of course, when I didn't have a nickel I could climb on the back of the 8th Avenue trolley and "hitch a ride" (that is, until the conductor chased me away). By the way, what can you buy for a nickel these days? Is there anything? And aside from taxes, why does the government still make pennies? Do you remember the expression, "a penny for your thoughts?" What would it be today, "a buck and a half for your thoughts?"

* *

Must one be big and strong and look like an athlete to be one? Hardly. On Aug. 16 a man ran the 5,000 meters 11 seconds faster than anyone in history. He was Ethiopia's Haile Gebreselassie, who ran the 5,000 meters in 10.91 seconds faster than the previous record of 12:55:30. In breaking the record, Gebreselassie reeled off the incredible equivalent of three 4:05 miles! Oh yes, Gebreselassie is five foot three and weighs 123 pounds. In winning the race in Zurich in world record time, he won a prize consisting of fifty thousand dollars and two pounds (not ounces, pounds) of gold (believe it, the Swiss know how to give meaningful prizes).

* *

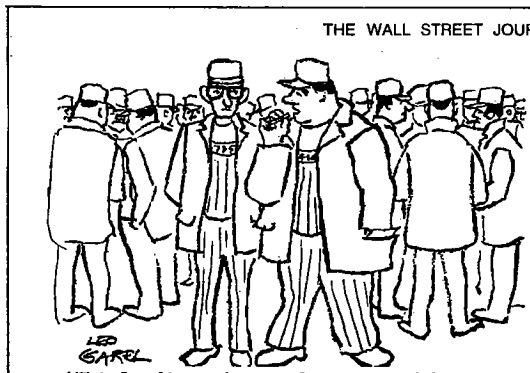
I thought the following was worth including. It's part of Haynes Johnson's marvelous piece about what World War II meant. It also describes a time when the US was the absolute most powerful nation in the world.

> Adm. Isoroku Yamamoto was one of the great commanders of World War II. Impassive in manner, deep in intellect, with broad shoulders and a thick chest, a man of practical sensibility and high sensitivity, he was both daring and prudent. No one among the Japanese high command was held in more esteem by those who served under him. None could claim to know the United States better than this officer who had studied at Harvard, served as a naval attaché in Washington, then planned the brilliant and stunningly successful attack on Pearl Harbor on Dec. 7, 1941. Yet even as his fleet steamed away from that victorious mission, Yamamoto had a premonition. "I fear," he said, "we have only succeeded in awakening a sleeping giant."
>
> The giant to which he referred was then held in contempt by Adolf Hitler, his Nazi commanders and most of the Japanese warlords. America was a weak, divided democracy, so they believed, a racially inferior "mongrel nation" incapable of uniting for full-scale global war and hopelessly ill-matched when confronted by incomparable German forces or fanatically determined Japanese soldiers, sailors and airmen.
>
> Sixteen months after Pearl Harbor, Yamamoto was dead, shot down April 18, 1943, by U.S. P-38s dispatched to intercept him. American intelligence had broken the Japanese codes and knew in advance not only his movements but those of the fleet he commanded, a fleet then in the process of being systematically destroyed by American naval and air forces. In two more years, Germany was in ruins, Hitler on the verge of committing suicide in his Berlin bunker.
>
> YAMAMOTO'S FEARS ABOUT THE SLEEPING GIANT had been realized.
>
> Socially, politically, economically, militarily, culturally, racially, sexually, demographically, even mythologically, World War II was the crucible that forged modern America. It was the transforming event that reshaped all who lived through it, and continues to affect those born after it. Only the American Revolution that created the new nation and the Civil War that preserved the Union rank with it in importance.
>
> For America, the energy unleashed by the war ended the lingering Great Depression of the 1930s and created an unmatched economic and technological colossus. It set in motion new laws that transformed the way we lived, bought homes, went to college. It changed the future for women and blacks at home, and produced both benevolence and arrogance abroad.

* *

I've been writing these Letters since December, 1958. During those 37 years I've seen a lot of market letters come and go. In speaking to a number of letter publishers over the past month, I gather this is about as tough a time as the industry has ever seen. One problem is the sheer amount of free information that is now disseminated via TV, radio, brokerage houses, newspapers, magazines and on-line. Another problem is that a bull market's on, and in bull markets (especially during periods of uninterrupted rises) people feel that they don't need advice.

But not to worry -- with it all, subscriptions here are holding up very well. And the new business I started is also doing extremely well. So it looks as though I'll be publishing *Dow Theory Letters* for a good while longer. The cartoon below hints at a rather different problem, however. Listen, I may make mistakes (don't we all), but (to repeat Richard Nixon's immortal line), "I am not a crook."



"I take it you're no longer writing your investment news letter?"

* *

Prices: Price of a seat on the NYSE two years ago was $600,000, half the level of 1987. In early August of this year a seat sold of $950,000. Some seats are leased; current price runs around $120,000 a year . . . Think that's high? A taxi medallion in NYC (required if you want to own a taxi) runs around $210,000. To cover the price, many taxis are run on two or even three shifts . . . Prices of some of the new fancy coffees run to $2.50 to even $3.50 a cup. I remember when coffee went from a nickel a cup to a dime (the price was raised when the price of the beans surged). To cover their embarrassment at raising prices, restaurants gave you refills at no cost. But today, many eateries even charge for refills.

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Diamonds: Small diamonds (under one carat) are increasingly common, while large gem-quality diamonds are increasingly rare. But there's trouble in the air. The Central Selling Organization (CSO) owned by giant De Beers has in the past literally controlled the diamond industry. However, Russia has been exporting large quantities of smaller or commercial grade diamonds to the West. If De Beers can't control the Russians, the system could break up into a two-tier system. De Beers would let the small diamond end of the business sink to its own level, while they would control the price of the gem-diamonds. Last month De Beers reduced the price of low quality rough (uncut) diamonds by 15% but at the same time they increased the price of high-grade stones by 2% to 8%. **Russell comment:** If a diamond price war was to break out, De Beers controls the price of the big, gem-grade diamonds and lets the commercial stones seek their own level. Remember, small (under one carat) diamonds are not rare, only large gem-quality diamonds are rare. You get almost nothing if you try to sell a small, chip-size diamond. Rubies are the rarest of gem stones, but emeralds and certain sapphires (Burmese, Kashmir) are also rare. Unlike diamonds, all *colored* stones are subject to free market prices of supply and demand .

'De Beers prepared for diamond price war'

By Kenneth Gooding, Mining Correspondent

A diamond price war and a big structural split in the rough

increases of 2 to 8 per cent on some high grade stones.

Analyst Mr Niall Carroll sees this as De Beers' response to unofficial Russian diamond

endure the consequences - the development of a price war and the disintegration of single channel marketing at the low end of the market.

ete a new marketing contract to replace one that ends in December. Mr Carroll says new reports suggest the Russians reacted angrily to the recent

"In other words, low end diamonds would become commodities. The downside risk is that such a strategy would damage the illusion, cultivated so

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The Aug. 20 *Sunday NY Times* contained an article which dealt with material which I thought was explosive (and almost

"politically non-correct"). The gist: *"Look collectively at the NY, Chicago, LA, Houston and Boston areas -- 5 of the top 11 immigration destinations. In the last half of the '80s, for every 10 immigrants who arrived, 9 residents left for points elsewhere. And most of those leaving were non-Hispanic whites. Of the major immigrant destinations, only metropolitan San Diego was attracting more whites from the rest of the nation than it was losing. The places the whites were bound for were metro areas like Tampa-St. Petersburg, Seattle, Phoenix, Atlanta, Las Vegas, all of which attract relatively few immigrants. The trend constitutes a new, larger form of white flight . . . This is reshaping America more and more into two nations. One is the rapidly changing coastal ports of entry such as San Francisco to Houston in the West, and Boston to Miami to Washington in the East along with Chicago. The second is the rest of the country . . . The force behind all this change is a decade of greater minority immigration than any in American history . . . Some 10 million legal and illegal immigrants entered the country in the '80s, exceeding the previous high of 9 million recorded in the first decade of the century . . . Moreover, unlike past eras of immigration, this new wave is more than 80% Latin and Asian . . . The No. 1 destination of blacks is Atlanta, the No. 1 destination of Hispanics is Miami, the No. 1 destination for Asians is LA . . . Within a decade California will be less than half white, with immigrants coming in and whites leaving. Whites are going mostly to neighboring states such as Washington, Oregon, Arizona."*

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Senator Bill Bradley is the sixth Senate Democrat to announce either retirement or a switch in parties this year, a modern record. If Dems lose even four seats in the coming election, they will have only 42 seats, the lowest number in 70 years. Said Walter Burnham, a scholar of political parties out of the University of Texas, *"The Democratic party has run out of options. This is part of a realignment sequence, one of those rare events most of us see maybe twice in a lifetime. It entails a collapse of their credibility, as far as I can judge."* **Russell comment:** I believe it represents the *people's judgment* on decades of the liberal welfare society, on inflation, on the decline of the family, of the collapse in morality. A large number of Americans have "had it" with the way things are going. They want change, real change. Clinton ran on a "change" ticket, but the only change we got was a change to *higher taxes.* The Republicans promise change, but so far they have delivered more talk than change. There are two major changes that the people want -- a *lot less* government and a *change in the tax system.* Those two items will, hopefully, represent the basic platform for the Republicans in '96.

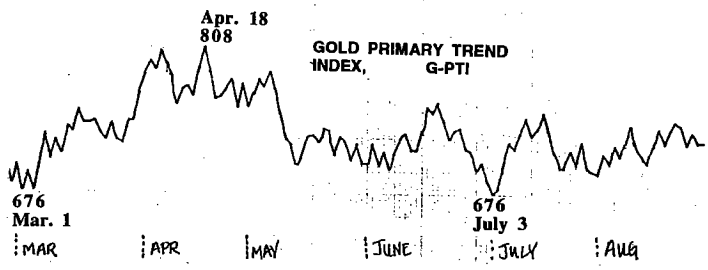
GOLD: At first I was skeptical, but the more I watch the action, the more I'm convinced that the central banks do NOT want gold above 400 and preferably NOT above 390. Every time gold appears ready to breech 390, whack, it gets hit. To my mind it's beyond coincidence. The central banks most definitely do not want to see a "bull signal" in gold.

Question: can the central banks keep gold down? We know that the money supply is now being pumped up in Japan. We know that the money supply figures are turning up sharply in the US. Other G-7 nations are loosening their money supply figures, as they seek to offset recessions or slowing business. Supposedly, this would put upward pressure on gold, but let gold get near 390 and WHAP! I say it's beyond coincidence.

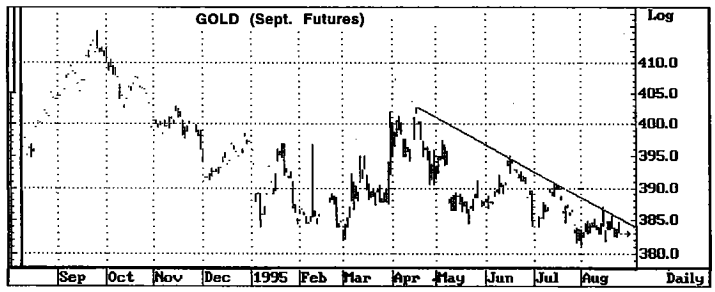
But in the end, the natural forces of supply and demand will win. They always do. In silver, there's an actual squeeze as demand pushes above supply. But central bankers don't worry about silver since the price of silver, in the public's mind, does not equate with inflation or deflation.

The daily chart of gold traces the rise in April in which gold pushed temporarily above 400. From then on, it's been declining peaks and lower lows -- on a perfect descending trendline basis. Good support appears at just above 380.

My Gold-Primary Trend Index (G-PTI) continues its weird, sideways meandering. Hardly exciting, but the G-PTI is doing its



job well -- accurately tracing out the underlying trend in gold (which is going nowhere).

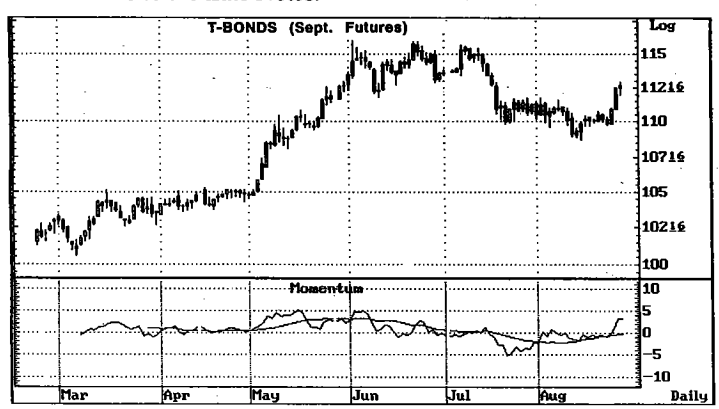


LATE NOTES: It's increasingly apparent -- a US and world economic slowdown is in progress. Listen to this from the excellent *Liscio Report* [(201)509-2256]: *"Let's put the economy in perspective. Durable goods orders have fallen in five of the past six months. Unfilled orders are lower now than they were in March. Industrial production fell in four of the past five months and would have been down in July if not for a big rise in utility output caused by hot weather. The past four months have produced fewer jobs than the average month did last year, and the back-to-school season could use some remedial buying."*

Germany with a slowing economy has just cut its rates again. Japan, as is well advertised, is in recession. France is wrestling with 12% unemployment, Spain's economy is slowing.

In the US we have an election coming up, and we have Greenspan itching to be reappointed as Fed head again. What to expect? It's obvious, the last thing the boys in Washington want is anything smacking of recession. Bank on it -- governments will fight oncoming recession tendencies with lower interest rates and expanding money supplies. Already the bond market has turned around strongly to the upside, and this is placing upward pressure on a stock market that "looked as if" it was topping out and in trouble. The trend to lower rates together with the now surging M-2 money supply will work against any trend towards weakness in the stock market. In the meantime, my PTI is breaking out to new highs, as is the advance-decline ratio. Note: remember, this Late Note section contains my *latest* thoughts, studies and instincts about the markets. Subscribers should always give precedence in these Letters to the Late Notes.

NEXT MAILING: Sept. 13, 1995



After reacting sharply, then consolidating, the bonds have broken out on the upside. They may be heading up to test the "triple top at the 115-116 area. Note the Bond Momentum index (bottom of chart) pushing above its moving average.